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## EDITORIAL

# Economic growth and poverty alleviation in Africa – linking hard and soft economics

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### Abstract

**Purpose** – The purpose of this editorial is to provide a quick glance at the dominant issues that have characterized the developing economics debate during the past five decades. It seeks to offer a backdrop for the papers in the present volume of *AJEMS*.

**Design/methodology/approach** – It is based on a review of a selection of literature that highlights the dominant perspectives in development economics.

**Findings** – It draws a distinction between soft and hard economics, arguing that economic growth must be converted into social change that benefits poor for it to be described as development-oriented.

**Originality/value** – It provides a direction for future research into issues of economic growth and poverty alleviation in Sub-Sahara Africa.

**Keywords** Poverty, Economic growth

**Paper type** Research paper

### Introduction

What is the nature and causes of economic progress and how is economic growth linked to poverty alleviation? These are some of the basic questions that leading economists have propounded theories and models to address during the last two and half centuries. Broadly speaking, the theories and models (as well as economic policies based on them) have been rooted in two contrasting paradigms. One is the neoclassical economic paradigm that gives support to the notion that economic systems can be likened to machines that transform inputs into outputs. The key drivers of economic progress are, therefore, symbolically described as “engines of growth”. I find it expositively appropriate to label this perspective as hard economics. The other paradigm sees economic decisions as social and political constructions that accommodate the intangible needs, expectations and behaviours of communities of people. It also emphasizes human capability development (including human capital) as a foundation of economic growth. I label this soft economics. The two paradigms, however, share the need for poverty alleviation in human societies, and agree with Robert McNamara’s description of poverty as “condition of life so degraded by disease, illiteracy, malnutrition and squalor as to deny its victims basic human necessities and a condition of life so common as to be the lot of some 40 per cent of the peoples of the developing countries”[1]. But they differ in their understanding of the roots of poverty and approaches to poverty alleviation.

The divergence in perspectives championed by the proponents of hard and soft economics is reflected in debates between leading development economists during the last half century. An example of this debate is between two leading Indian economists – Amartya Sen and Jagdish Bhagwati. While Sen (1981) believes that India should invest more in its social infrastructure (including health and education) to improve



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human capabilities as prerequisites for increased productivity and growth, Bhagwati argues that only a focus on growth can yield enough resources for investing in social sector schemes – i.e. seeing growth as a prerequisite for social development (see Bhagwati and Panagariya, 2013). In a similar vein, Alfred Hirschman and Paul Streeten forcefully debated the concept of balance and un-balanced growth in the 1960s (Alacevich, 2011). Hirschman (1963) proposed a distinction between “social overhead capital” (SOC) and “directly productive activities” (DPA). In his view, a well-developed SOC in a country or community is a precondition for DPAs. He included all public services (from law and order through education and public health to transportation, communications, power and water supply, as well as such agricultural overhead capital as irrigation and drainage systems) in his concept of SOC (Alacevich, 2011).

These discussions have inspired debates about the links between economic growth and economic development. Following Hirschman (1963), the term “economic development” implies the process of change from a less developed type of economy into some other more advanced type. Implicit in his understanding and those of many other development economists is that development results in poverty alleviation. It also connotes the goal of “enlarging people’s choices in a way which enables them to lead longer, healthier and fuller lives” (Ranis *et al.*, 2000, p. 197). In other words, development provides a qualitative interpretation of economic growth – i.e. growth must be converted into social change that benefits poor for it to be described as development-oriented. The prevailing understanding therefore is that there is a dual link between economic growth and economic development – economic development provides the necessary conditions for economic growth and growth produces resources necessary for economic development. As an end in itself, it is considered socially and politically inexcusable (in the long run) to pursue growth at the expense of development.

Placing this debate in the Sub-Sahara African (SSA) context, it is important to note that until barely a decade ago, both academic and journalistic analysts have pronounced SSA a hopeless case of economic growth and development experiments. As Kariuki and Najam (2011, p. 100) informs, the prevalent narratives have followed the pattern of “bursts of peaking global interest (optimism), followed by periods of global neglect (pessimism); recognition of continental potential, followed by litanies of despair and dismay; expressions of great expectations, followed by prognoses of hopelessness”.

There have been justifications for the persistent pessimism registered by contributors to the debate. The available evidence shows that only six SSA countries have more than tripled their per capita incomes between 1960 and 2005, nine have per capita incomes equal to or less than where they started in 1960 and the rest have seen some net improvement, but not enough to make any real dent in their poverty levels. Those countries that showed promises of fast growth in the 1970s (e.g. Côte d’Ivoire) faced stagnation or even decline during a greater part of the past five decades. Furthermore, until the beginning of the twenty-first century, investment in most African countries yielded less than half the return measured in growth terms than in other developing regions.

Fortunately, there have been some positive signs of economic turnaround in some African countries during the past decade. Real GDP rose by 4.9 per cent a year from 2000 through 2008, more than twice its pace in the 1980s and 1990s. Africa’s collective GDP was estimated to be at \$1.6 trillion in 2008. Although a remarkable improvement in an African context, this figure barely equals the GDP of countries such as Russia and Brazil. But the sub-continent is now among the world’s most rapidly growing economic regions. Many observers and well-wishers agree that this acceleration is a sign of hard-earned progress and promise. The challenge again is the sustainability of

the new positive economic experience. Some scholars have warned that previous periods of rapid growth across Africa have often been followed by phases of economic decline which have erased many of the gains countries have achieved in per capita income. The continent's transition to modern economic growth will thus require a break in the boom-and-bust pattern which has characterized its economic performance during much of the twentieth century (Broadberry and Gardner, 2013).

Furthermore, although the records show impressive gains in hard economics terms, the gains in soft economics appear to be weak. Jobs are not being created, sufficient health services are not being provided and the incidence of inequality has not been reduced in most countries. Even the most optimistic assessments indicate that the prospects of achieving the Millennium Development Goals in SSA by the target year 2015 remain bleak.

It is in the light of the above discussions that the collection of papers in this volume of *AJEMS* must be read. Together, they make thoughtful contributions to the debate on the determinants of economic growth and how they should be balanced with development – i.e. the indicators of well being of the citizens of individual African countries.

Simplicé Asongu's paper is entitled "Are proposed African monetary unions optimal currency areas? Real, monetary and fiscal policy convergence analysis". It takes up the issue of financial capital management that is considered one of the key resources in hard economics and an important economic growth factor. In the language of economists, Economic and Monetary Union may be considered an umbrella construct describing a group of policies aimed at some degree of economic convergence among nations forming the union. This may involve the adoption of a common currency and/or adherence to a single monetary and exchange rate policy. The nations forming the union normally agree on a threshold level of convergence of their diverse monetary and fiscal policies before the union takes effect. Part of this convergence arrangement involves considerations as to levels of inflation, interest rate and foreign exchange rates as well as budget deficit and levels of public debt of individual member states. These arrangements are meant to maintain acceptable degree of disciplined nation-level fiscal and monetary policies and avoid undesirable spillover effects between member states.

Asongu's study was motivated by the author's awareness that the introduction of common currencies in West and East Africa has been facing challenges in the timing of monetary convergence. Thus, it aimed at assessing "real, monetary and fiscal policy convergence within the proposed WAM and EAM zones". He used a "dynamic panel GMM estimation with data from different non-overlapping intervals" to compute optimal rate of convergence and the time required to achieve full convergence that will ensure the preservation of the anticipated stability of the monetary union. The results suggest overwhelming lack of convergence: initial conditions for financial development were found to be different across countries; such fundamental characteristics as common monetary policy initiatives appeared to be implemented differently across countries; there were cross-country variations in structural characteristics of macroeconomic performance; and there was an evident absence of fiscal policy convergence.

Anthony Adu-Asare Idun's paper also contributes to the finance capital debate. It builds on the common understanding within the economic growth literature that the level of financial market development has an impact on the economy of a nation. Evidence from both single-country and cross-country studies suggests that economies with more developed financial markets tended to grow earlier, attain higher growth rates and achieve higher levels of per capita income than economies with less-developed

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financial markets (Mitchener and Wheelock, 2012). Empirical evidence also suggests that financial intermediaries improve resource allocation and fund projects with higher rates of return by matching borrowers and lenders efficiently (Kashyap *et al.*, 2002).

Motivated by this view, governments in most African countries, including Ghana began to implement financial sector reforms starting in the late 1980s as part of their broad market reforms. The major goals of these reforms were to build more efficient, competitive robust and deeper financial markets. Key aspect of the reforms included the deregulation of the financial sub-sector through privatization of state-owned banks, increasing the number of private banks and registration of non-bank financial institutions.

The study reported in the paper takes the finance-growth nexus further by looking at the relationship between bank competition, financial innovations and economic growth in Ghana. The empirical investigation is based on quarterly data from 1990 to 2009 and adopts endogenous growth model and cointegration procedures to explore the relationships. The results show that, in the long run, bank competition is positively related to economic growth while financial innovation is negatively related to economic growth.

One aspect of soft economics is the link between health care services and productivity. Health economists argue that there is increasing returns from health expenditures in developing countries in terms of increasing values in productivity as well as increased social benefits. The benefits are even more pronounced with improvement in child health services. Studies have also found that there is a strong link between favourable child health outcomes on the one hand, and child nutrition (Frosta *et al.*, 2005). This issue is explored in Edward Bbaale's study entitled "Maternal education and child nutritional status: evidence from Uganda". The focus on parental (especially women) education and child health care is particularly important. The prevailing understanding in the health care literature is that educated women have greater knowledge of diseases and modern health care services and have greater ability and confidence to discuss their children's health concerns with health-care providers (Barrera, 1990). Furthermore, maternal education has a significant and independent influence on child nutritional status (Frosta *et al.*, 2005). Bbaale's study corroborates this understanding with evidence from Uganda. For example, if mothers are educated beyond secondary level their influence on child nutrition becomes greater than those at relatively lower levels of education. Furthermore, children of low- and semi-skilled employed Ugandan mothers appear to have poorer child nutrition status than non-working mothers.

Bernardin Senadza also takes up a soft economics issue in his paper "Income diversification strategies among rural households in developing countries: evidence from Ghana" examining the determinants of households' choice of income portfolio. The study adopted a multinomial logit approach with results showing that such factors as household characteristics, location and infrastructure influence Ghanaian rural household members' income strategy choices. Education and access to credit and electricity also seem to influence people's ability to generate income through non-farm economic activities. This study therefore reinforces the issues and conclusions from Bbaale's study that parental education and income impact child nutrition, health and welfare and contribute indirectly to a nation's economic growth.

It has been argued above that sustainable economic growth relies on the ability of economies to generate jobs and livelihoods on an ongoing basis. Many believe that this is better done by private enterprises than state-owned companies in SSA.

But companies located in these countries (local and foreign) must be mindful of local needs and must be willing to keep their workers healthy, well informed and motivated and help them build a viable society – in a word, they must be socially responsible. Making capitalism serve the poor has therefore become a noble cause that has been propagated by wealthy individuals such as Bill Gates.

Richard B. Nyuur, Daniel F. Ofori and Yaw Debrah dwell on this theme in their paper “Corporate social responsibility in Sub-Saharan Africa: hindering and supporting factors”. The relevance of the paper must be seen in the light of the fact that while considerable research has been conducted on CSR in developed countries, the extant literature on CSR in SSA is scant and CSR is seen only in terms of philanthropy. The study builds on the available literature in the field and extends it further by identifying factors that hinder and promote CSR activities in SSA, using data obtained from a survey conducted by GTZ (now GIZ).

The results identify nine key promoting and hindering factors of CSR in the countries covered. These include: leadership and governance, policy framework, project management, monitoring, evaluation and reporting, stakeholder engagement, staff engagement, government, funding and beneficitation. The authors suggest the adoption of formal and informal dialogues and engagement practices with key stakeholders within specific communities in which businesses are located in order to relate CSR practices more directly to the developmental needs of the communities. They also advise management to link their CSR activities to areas that improve firms’ long-term competitive potential by collectively and systematically applying their distinctive strengths to such activities. The underlying argument is that companies create business and societal value when they take a broader and longer-term view of their business activities. This conclusion is in line with Michael Porter and Mark Kramer’s concept of creating shared value which holds that corporations can be vastly more effective than individuals in addressing social issues, because corporations have relevant expertise and resources far beyond those of individuals (Porter and Kramer, 2011).

The zone of contest between hard and soft economics is further illustrated in Monal Abdel-Baki’s paper which discusses “The nexus between monetary policy and housing in Egypt and South Africa”. The study compares and contrasts the effectiveness of monetary policy in boosting the housing sectors in the two countries – Egypt and South Africa. It adopts “an eight-variate two-stage structural vector autoregressive model” to compare the efficacy of monetary policy between 1975 and 2010. The results show that the impact of monetary policy on the housing sector has not been not uniformly effective. In economies with more developed mortgage markets, like South Africa, monetary agents can affect credit availability than in countries with weak mortgage markets.

The volume also contains “practitioner viewpoint” papers. The first is by Brian Kampanje using “PESTEL” framework to analyse Malawi’s non-life insurance industry. Kampanje argues that both life and non-life insurance have a positive and significant causal effect on economic growth in terms of mobilizing domestic savings; improving the efficient management of different types of risks, thereby encouraging the accumulation of new capital; improving financial stability; fostering a more efficient allocation of domestic capital. But while the life insurance industry in African countries (including Malawi) is favoured by employment and pension laws, giving them protected market access, the non-life insurance sector is usually administered on voluntary basis. Not only do government policies disadvantage the non-life insurance sector, it also exposes citizens to greater risks. Here again, level of education is found to

be a key instrument of growth. Education promotes financial literacy and risk awareness, and thereby stimulates of peoples' demand for non-life risk insurance services.

Put together, these studies reconfirm the view that economic progress is not a spontaneous act driven by God-like invisible hands. It requires deliberate and proactive facilitation. The process may sometimes be messy. But without some kind of facilitation, the theoretical links between economic growth and development suggested in the literature may never materialize in some countries or may happen rather slowly and may fail to fulfill the expectations of citizens.

Furthermore, policymakers must strive to find ways of making sensible trade-offs between "pro-growth" and "pro-poor" policies – i.e. balancing citizen's need for manifest welfare gains as well as enterprises' need to fulfil shareholder expectations. Research is still required in individual African countries and within regions of the sub-continent to determine what types of growth policies can help poor people most in a given environment and to determine the extent to which public spending on social services may crowd out growth-oriented sectors within those individual countries.

#### Note

1. This description was contained in a speech that Robert McNamara gave in Nairobi, Kenya in 1993 (see Alacevich, 2011).

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